IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF DELAWARE

MILTON PFEIFFER,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Civ. No. 04-296-SLR
	)	
SOL PRICE,	)	
	)	
Defendant, and	)	
	)	
	)	
PRICESMART, INC.,	)	
	)	
Nominal Defendant.	)	

MEMORANDUM ORDER

I. INTRODUCTION

This case presents the question of whether the defendant's sale and subsequent acquisition of equity securities issued by the PriceSmart Corporation triggered the short-swing profits capture provision of Section 16(b) of the Security Exchange Act of 1934, 15 U.S.C. § 78(p)(b)[1] ("Section 16(b)"). On May 17,

[1]Section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78p(b), states:

For the purpose of preventing the unfair use of information which may have been obtained by such (more than 10%) beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, unless such security was acquired in good faith in connection with a debt previously contracted, shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in

2004, plaintiff Milton Pfeiffer ("plaintiff"), as a shareholder of the PriceSmart Corporation,[2] brought this derivative action against defendant Sol Price ("defendant") in which plaintiff seeks disgorgement of short-swing insider profits allegedly realized by defendant. (D.I. 1) Defendant thereafter challenged the suitability of the requested relief by filing a motion to dismiss plaintiff's complaint pursuant to Federal Rules of Civil Procedure 12(b)(6). (D.I. 7) Because plaintiff has satisfied the minimal pleading requirements needed to overcome a 12(b)(6) motion and relief could be granted under any set of facts consistent with the allegations of the complaint, defendant's motion to dismiss is denied.

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entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. Suit to recover such profit may be instituted at law or in equity in any court of competent jurisdiction by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request or shall fail diligently to prosecute the same thereafter; but no such suit shall be brought more than two years after the date such profit was realized. This subsection shall not be construed to cover any transaction where such beneficial owner was not such both at the time of the purchase and sale, or the sale and purchase, of the security involved, or any transaction or transactions which the Commission by rules and regulations may exempt as not comprehended within the purpose of this subsection.

[2]PriceSmart was named in the plaintiff's complaint as a nominal defendant (D.I. 1) and has adopted the arguments set forth in the Opening Brief of defendant Sol Price in support of its motion to dismiss (D.I. 9).

II. BACKGROUND

Both parties agree that in April of 2003, defendant Sol Price, as trustee of the Price Family Charitable Trust ("Charitable Trust"), executed a purchase agreement ("April Agreement") with the San Diego Revitalization Corporation ("SDRC") that effectuated a sale of 619,046 shares of PriceSmart common stock from the Charitable Trust to the SDRC for $950,000 in cash and the remaining balance in a non-recourse note.[3] (D.I. 8) The price of the stock involved in the April Agreement was $16.12 per share, totaling $9,979,021.52. (D.I. 8, Ex. B) The April Agreement was executed on the 24th of that month, with the actual transfer of the purchased shares occurring the following day. (D.I. 8) The April Agreement provided no material conditions to closing and, as such, created irrevocable obligations on both the Charitable Trust and the SDRC to fulfill the terms of the agreement. (D.I. 8, Ex. B) The non-recourse note was secured by a pledge agreement which enables the Charitable Trust to reacquire the shares in the event the SDRC defaults on its payments under the loan. Id.

In addition to his involvement in the Charitable Trust, the defendant serves as trustee of the Sol and Helen Price Trust

[3]The non-recourse promissory note, in the principal amount of $9,029,021.52, is stated in the April Agreement as having accounted for over ninety percent of the purchase price and is chargeable to defendant in April of 2008. (D.I. 8, n. 4; Ex. B)

("Family Trust"). Id. In October of 2003, the Family Trust entered into a purchase agreement ("October Agreement") with nominal defendant PriceSmart to purchase 330,000 shares of PriceSmart common stock for $10.00 per share. Id. On December 12, 2003, plaintiff, as required by Section 16(b), demanded that the PriceSmart Board of Directors justify the allegedly improper transactions concerning defendant or commence an action against defendant to disgorge the short-swing profits if a violation is found to have occurred. (D.I. 12) As evidenced by this lawsuit, the Board of Directors, after investigating the matter, found plaintiff's claims to be without merit. (D.I. 8) The Board of Directors responded to plaintiff's demand letter on February 10, 2004, arguing that: (1) the two transactions at issue did not occur within six months of each other; (2) that the defendant did not actually have a pecuniary interest in the securities held by either the Charitable Trust or the Family Trust; and (3) that for purposes of Section 16(b) liability, the April and October transactions did not result in a profit. Id. On May 17, 2004, plaintiff filed the present lawsuit, alleging that defendant, as trustee of the Charitable and Family Trusts, profited from the sale and subsequent purchase of PriceSmart stock within a six month period in clear violation of 16(b). (D.I. 1)

Defendant subsequently filed the present motion to dismiss on July 1, 2004. (D.I. 7) Mirroring the substantive legal

arguments that were put forth by the PriceSmart Board of Directors, defendant argues in his motion to dismiss that plaintiff's complaint fails to adequately allege sufficient facts to prove a violation of Section 16(b). Id. Specifically, defendant contends that: (1) the parties to the April transaction were irrevocably bound on April 24, 2003 despite the transfer of stock the following day; (2) the parties to the October transaction were not irrevocably bound until the transaction closed on October 23, 2003;(3) plaintiff has failed to allege any facts that would allow the court to conclude that defendant was a "beneficial owner" of the stock at issue in the April or the October transactions; and finally (4) plaintiff failed to properly allege that defendant realized a profit from the two transactions. (D.I. 8, 13)

In response, plaintiff alleges that the parties to the April and October transactions became irrevocably committed on April 25, 2003 and October 22, 2003, respectively. (D.I. 12) Accordingly, plaintiff argues, the sale and subsequent purchase of PriceSmart securities were within the statutory six month period and constituted a violation of 16(b). Id. Moreover, plaintiff alleges that defendant was a beneficial owner for purposes of 16(b) liability and that the complaint adequately alleges that defendant profited from the April and October transactions. (D.I. 8)

III. STANDARD OF REVIEW

In analyzing a motion to dismiss pursuant to Rule 12(b)(6), the court must accept as true all material allegations of the complaint and it must construe the complaint in favor of the plaintiff. See Trump Hotels & Casino Resorts, Inc. v. Mirage Resorts, Inc., 140 F.3d 478, 483 (3rd Cir. 1998). "A complaint should be dismissed only if, after accepting as true all of the facts alleged in the complaint, and drawing all reasonable inferences in the plaintiff's favor, no relief could be granted under any set of facts consistent with the allegations of the complaint." Id. Claims may be dismissed pursuant to a Rule 12(b)(6) motion only if the plaintiff cannot demonstrate any set of facts that would entitle him to relief. See Conley v. Gibson, 355 U.S. 41, 45-46 (1957). The moving party has the burden of persuasion. See Kehr Packages, Inc. v. Fidelcor, Inc., 926 F.2d 1406, 1409 (3rd Cir. 1991). "The issue is not whether a plaintiff will ultimately prevail but whether the claimant is entitled to offer evidence to support the claims." In re Burlington Coat Factory, Sec. Litig., 114 F.3d 1410, 1426 (3rd Cir. 1997).

It must also be noted that the court is not relying on matters outside the pleadings to decide this motion. Defendant is correct in referencing the April and October agreements without running the risk of converting his motion to dismiss into

one for summary judgment. (D.I. 8) See also In re Burlington, 114 F.3d at 1426("'document[s] integral to or explicitly relied upon in the complaint' may be considered 'without converting the motion [to dismiss] into one for summary judgment.'")(citations omitted).

IV. DISCUSSION

Section 16(b) of the Exchange Act requires that any profits realized from the purchase and sale (or vice versa) of securities by persons deemed to be insiders within a six month period be disgorged to the issuer of the securities. "Insider" is defined by the statute as a beneficial owner of more than ten percent of any class of the corporation's non-exempt, registered equity securities, or a director or officer of the company issuing the stock. 15 U.S.C. §78p(a-b). For pleading purposes, the elements of a Section 16(b) claim are: "(1) a purchase and (2) a sale of securities (3) by . . . a shareholder who owns more than ten percent of any one class of the issuer's securities (4) within a six-month period." Global Intellicom, Inc. v. Thomson Kernaghan & Co., 1999 U.S. Dist. LEXIS 11378 (D.N.Y.1999)(quoting Gwozdzinsky v. Zell/Chilmark Fund L.P., 156 F.3d 305, 308 (2nd Cir. 1998).

Defendant's motion to dismiss appears to place much emphasis on plaintiff's failure to plead with specificity the elements of the Section 16(b) cause of action. This court, however, has held

that the pleading standard that governs Section 16(b) is not the heightened pleading standard of Fed. R. Civ. P. 9(b) but rather the notice pleading requirements of Fed. R. Civ. P. 8.[4] Rosenberg v. XM Ventures, 129 F. Supp.2d 681, 686 (D. Del. 2001). Although courts generally apply the heightened pleading standard of Rule 9(b) to causes of action alleging a violation of Sections 10(b) and 10(b)-5 of the Exchange Act, Rule 9(b) "is to be applied narrowly and not to legal theories other than those based on fraud or mistake." Mayer v. Chesapeake Ins. Co., 1987 U.S. Dist. LEXIS 681, *8 (S.D.N.Y. February 3, 1987). Defendant himself cites to cases in his reply brief that make the distinction between the pleading standard for 16(b) actions and 10(b) and 10(b)-5 actions. (D.I. 13, Ex. A)(citing Global Intellicom v. Thompson Kernaghan & Co., 1999 WL 544708 (S.D.N.Y. July 27, 1999)). A successful claim under 16(b) does not depend on the elements of fraud for its application and, therefore, this court does not require application of Rule 9(b) when analyzing a 16(b) claim for purposes of a motion to dismiss.

[4]Rule 8 states in relevant part: "A pleading which sets forth a claim for relief, whether an original claim, counterclaim, cross-claim, or third-party claim, shall contain (1) a short and plain statement of the grounds upon which the court's jurisdiction depends...(2) a short and plain statement of the claim showing that the pleader is entitled to relief, and (3) a demand for judgment for the relief the pleader seeks." Fed. R. Civ. P. 8. In contrast, Rule 9(b) sets forth a heightened pleading standard that requires all averments to be plead with particularity where the claim concerns special matters involving fraud, mistake, or condition of the mind. Fed. R. Civ. P. 9(b).

With this standard in mind, the court now looks to the merits of defendant's motion to dismiss.

A. The April Transaction

Defendant contends that the April transaction, for purposes of 16(b) liability, irrevocably committed the Charitable Trust to consummate the sale of 619,046 shares of PriceSmart common stock to the SDRC on April 24, 2003, the date of closing specified in the Purchase and Sale Agreement. (D.I. 8, Ex. B) The court agrees. "The technicalities of stock transfers, such as the passing of title or the exchange of the shares are, by themselves, of no import for § 16(b) purposes." Prager v. Sylvestri, 449 F. Supp. 425, 432-433 (S.D.N.Y., 1978); See also Provident Securities Co. v. Foremost-McKesson, 506 F.2d 601, 606 (9th Cir. 1974); Blau v. Ogsbury, 210 F.2d 426, 427 (2nd Cir. 1954); Foremost-McKesson v. Provident Securities Co., 423 U.S. 232, 254 at n.28 (1974)("[As] a matter of practicalities the crucial point in the acquisition of securities is not the technical 'purchase,' but rather the decision to make an acquisition"). Moreover, because the April transaction contained no material conditions to closing, defendant did not have "the power to affect when the transfer would occur." Prager, 449 F. Supp. at 435. Plaintiff's assertion, that the failure to deliver the actual shares until the following day invalidated the Purchase Agreement, is without merit. Accordingly, this court

finds that the April transaction irrevocably committed the defendant to sell the shares on April 24, 2003.

B. The October Transaction

Defendant next contends that the October transaction created the requisite irrevocable commitment to purchase the shares on October 23, 2003. Plaintiff, however, counters with the assertion that the October purchase occurred a day earlier. As such, the October transaction can only give rise to 16(b) liability if an irrevocable commitment to purchase PriceSmart common stock by defendant was created on or before October 22, 2003.[5]

The primary argument of defendant is that the October transaction contained material conditions to closing and that, as a result, the conditions were not fulfilled until the actual closing on October 23, 2003. Defendant is correct in noting that, where there is a material condition to closing, the closing date (and not the execution or signing date) is the date that

[5]"[A] period of less than six months [means] a period the first and last days of which each include the twenty-four hours from midnight to midnight, and the last day of which is the second day prior to the date corresponding numerically to that of the first day of the period in the sixth succeeding month. For example, the period from and including January 1st to and including June 29th would be a 'period of less than six months' but the period to and including June 30th would be a period of exactly six months. Thus profit realized from a purchase on January 1st and a sale on June 30th would not be recoverable under the statute. See Stella v. Graham-Paige Motors Corp., 132 F. Supp. 11, 103-04 (S.D.N.Y. 1955).

irrevocably commits the parties to the transaction. Brenner v. Career Acad., Inc., 467 F.2d 1080 (7th Cir. 1972); Portnoy v. Revlon, Inc., 650 F.2d 895, 900 (7th Cir. 1981). Defendant cites to three provisions[6] of the October Agreement and asks this court to rule, as a matter of law, that the provisions are material conditions to the consummation of the October transaction. Defendant relies on a California state case for the proposition that boilerplate language can contain material contingencies and, as such, the October Agreement contains material contingencies that preclude a finding that the parties were irrevocably committed to consummate the transaction until the closing on October 23, 2003. (D.I. 13) This reliance is misplaced.

In Regency Wines, Inc., v. Champagne Montaudon, 2002 WL 31788972 (Cal. App. 2d Dist. Dec. 13, 2002), the court held that a forum selection clause found in Montaudon's invoices

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[6]Defendant argues that the material conditions in the October Agreement include:
(1) No event shall have occurred and no condition shall have arisen or been created since the date of th[e] Agreement which has had, or would be reasonably likely to have, a Material Adverse Effect [on PriceSmart]" (October Agreement § 7.6);
(2) The representations and warranties of each of the parties was to be true and correct as of the closing date (§§ 7.1 & 8.1);
(3) There was to be no litigation pending or threatened wherein an unfavorable injunction, judgment, order, decree, ruling or charge would (i) prevent, materially delay, prohibit or otherwise make illegal the consummation of the transactions by the October Agreement, (ii) cause a rescission of any such transaction after consummation, or (iii) adversely affect the right of the Family Trust to own the stock purchased in the October Transaction (§§ 7.3, 8.3). (D.I. 8, Ex. C)

constituted an additional term to the original contract and materially altered the original contract as a matter of law. Id. at *7. The Regency court stressed that the forum selection clause at issue "may result in the relinquishment of significant procedural rights...[that] would result in surprise or hardship if incorporated without express awareness by the other party." Id. In the case at bar, there is no surprise or hardship to the defendant because the provisions alluded to by defendant in his brief were already included in the original contract between defendant and PriceSmart. (D.I. 8, Ex. C)

The court concludes that the standard contract language cited by defendant does not constitute, as a matter of law, material conditions precedent to closing the transaction at bar. The parties will have the opportunity, through discovery, to demonstrate that the underlying facts of the transaction known by both parties warrant a different characterization of these conditions precedent. Accordingly, the court holds that defendant has failed to meet his burden of proving that the October Agreement irrevocably committed the parties to consummate the October transaction after October 22, 2003. See Kehr Packages, Inc. v. Fidelcor, Inc., 926 F.2d 1406, 1409 (3rd Cir. 1991).

C. Beneficial Ownership Under Section 16(b)

Defendant next contends that plaintiff's complaint is

fatally flawed due to a failure to properly allege that defendant, as a beneficial owner of the PriceSmart common stock at issue in the two transactions, had a pecuniary interest in the securities held by the Charitable Trust or Family Trust. (D.I. 8) Plaintiff counters that his complaint properly alleges that "defendant Price illegally collected more than $2 million in short-swing trading profits in violation of Section 16(b)." (D.I. 1) In the event the complaint is found deficient on this point, plaintiff seeks leave to amend the complaint.[7] (D.I. 12, Fn. 7)

Defendant is correct in noting that Section 16(b) defines "beneficial ownership" as "any person, who directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, has or shares a direct or indirect pecuniary interest[8] in the equity securities." 15 U.S.C.

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[7]"A party may amend the party's pleading once as a matter of course at anytime before a responsive pleading is served. . . ." Fed. R. Civ. P. 15(a). Neither a motion to dismiss nor a motion for summary judgment constitutes a responsive pleading under Fed. R. Civ. P. 15(a). Apple Computer, Inc. v. Unova, Inc., 2003 U.S. Dist. LEXIS 23843 (D. Del. November 25, 2003). "Otherwise a party may amend the party's pleading only by leave of court or by written consent of the adverse party. . . ." Id. Though motions to amend are to be liberally granted, a district court "may properly deny leave to amend where the amendment would not withstand a motion to dismiss." Centifanti v. Nix, 865 F.2d 1422, 1431 (3rd Cir. 1989).

[8]Pecuniary interest is defined as "the opportunity, directly or indirectly, to profit or share in any profit derived from a transaction in the subject securities." 17 C.F.R. §240.16a-1(a)(2)(i)(2004).

§78p(a). Although the power to vote or sell shares may constitute beneficial ownership pursuant to Section 16(b), "[i]t is clear...that control without direct financial interest does not constitute beneficial ownership." Mendell on Behalf of Viacom, Inc. v. Gollust, 793 F. Supp. 474, 480 (S.D.N.Y. 1992). Plaintiff's complaint is flawed because he assumes that defendant, as a trustee of the Charitable and Family Trusts, is a fortiori a beneficial owner of the securities held by those trusts. The plaintiff, however, requested in the alternative for leave of court to amend his complaint to remedy this portion of his complaint in the event the court finds it deficient. (D.I. 12, Fn. 7) Accordingly, because defendant failed in his reply brief to challenge plaintiff's alternative request to amend the complaint, plaintiff's request for leave to amend is granted.

D. Plaintiff Properly Alleged A Profit For Purposes Of Section 16(b)

Lastly, defendant contends that plaintiff's complaint should be dismissed because plaintiff "must allege that the value of the consideration generated a profit." (D.I. 8) Specifically, defendant argues that the profit alleged in the complaint fails to take into account the true value of the nonrecourse note used in the April transaction, the value of which must be discounted to reflect the risk associated with being able to collect the consideration. Id.

As stated earlier, the elements of a claim under Section 16(b) are that "there was (1) a purchase and (2) a sale of securities (3) by an officer or director of the issuer or by a shareholder who owns more than ten percent of any one class of the issuer's securities (4) within a six-month period." Gwozdzinsky v. Zell/Chilmark Fund, L.P., 156 F.3d 305, 308 (2nd Cir. 1998). A plaintiff must allege, at a minimum, "that [defendant] realized short-swing profits" in order to survive a motion to dismiss. See Margolies v. Rea Brothers Plc., et al, 1983 WL 1333 (S.D.N.Y. June 30, 1983)(dismissing complaint because defendant failed to allege short-swing profits). In his complaint, it is undisputed that plaintiff alleged that defendant realized illegal short-swing profits from the purchase and subsequent sale of PriceSmart securities. (D.I. 1) For purposes of a 12(b)(6) motion to dismiss, plaintiff's complaint passes muster[9] under Rule 8(a).

[9]Defendant, in arguing that plaintiff's complaint requires "more particular pleadings" (D.I. 13), relies on Allis-Chalmers Mfg. Co. v. Gulf & Western Indus., Inc., 527 F.2d 335, 352 (7th Cir. 1975). In Allis-Chalmers, the appeals court analyzed the plaintiff's evidence of the consideration received in the sale leg of the short swing transaction at issue, holding that "in transactions involving debt obligations of an amount certain, evidence of payment in full, if available at the time of trial, should control the determination of 'profit realized.'" Allis-Chalmers, 527 F.2d at 357 (emphasis added). Again, defendant's reliance on case law that sets forth what is necessary for a plaintiff to prevail in an action under Section 16(b) is inappropriate at this stage in the proceedings. In his reply brief in support of his motion to dismiss, defendant himself alludes to the Allis-Chalmers court's finding at trial that the

V. CONCLUSION

At Wilmington this 27th day of December, 2004;

IT IS ORDERED that:

1. Defendant's motion to dismiss (D.I. 7) is denied.

2. Plaintiff's request for leave to amend the complaint is granted.

Sue L. Robinson
United States District Judge

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lower court erred in finding for the plaintiff on the issue of valuation of the risk associated with a sale by note. (D.I. 13)

While defendant's arguments concerning the proper valuation of the non-recourse note used in the April transaction may prove persuasive at a later point, plaintiff's complaint cannot be said to be fatally flawed for not going beyond Rule 8(a) and pleading with particularity.